

PEARLSTEIN'S CORNER

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Mark Pearlstein

VP, Portfolio Manager &
Wealth Advisor

416.733.5257

mark.pearlstein@rbc.com

www.markpearlsteinwealthmanagement.com

3 Ways How Brexit May Affect Your Life Style in Canada

I woke up at 4:00am on June 24th to a big surprise. Brexit – short for British exit - happened. Contrary to what most pundits assumed, a majority of U.K. voters felt they'd be better off economically with more control over their sovereignty by leaving the European Union (EU) - 28 European countries that allows for free movement of goods, services, money and people. **A key reason for Leave side winning; over half of the U.K.'s laws and regulations are currently written in Brussels. Immediately after the referendum stock markets shuttered all over the world.**

1. A small short-term stock trade on Brexit won't impact your life style

A new client Edward, a former Londoner, wanted to make money on the uncertainty caused by Brexit. He called me at 6:30 am. "If there's a big down turn in the stock market, I want to buy the dip and then sell." I called him after the market opened saying his big opportunity didn't happen because the markets had already discounted a very important detail. It's going to take at least several years for Britain to leave the EU.

Now there's nothing wrong with short-term trading which is speculating as opposed to long-term investing; it's just so hard to do. Your odds of making money is about one in five or 20%. And it's not part of my practice.

2. Brexit can help to keep the price of your house climbing

How? Interest rates in Canada actually dropped after Brexit. Global uncertainty helps to keep interest rates low, keeping mortgage rates low, fanning the flames in our hot housing market. Also, low rates keep the Canadian dollar weak, attracting more foreign buyers to politically stable Canada. One of the reasons Edward wanted to trade stocks was with interest rates being so low, he felt he would not make enough of a return on fixed income investments.

3. Brexit can impact your life style depending on your asset allocation since Brexit is a symptom of a slow growth world

Edward not only likes to trade stocks, it seems he likes them so much since his portfolio of \$2 million is 100% stocks. He and his wife Jill are retired but there's no room for error should the markets decline at some point. While no short-term stock trade happened, I did book a meeting to review their portfolio with a long-term view in mind. As part of my practice with all new clients, we built out their 'Peak Life Style'. **Peak Life Style is simply the life you want to live in retirement whatever you imagine it to be.** Edward and Jill are in their mid 60's and their adult children are well established. They own a mortgage-free home in Toronto and enjoy active, full lives. They draw pensions from several sources but are careful with their spending.

Their asset allocation needed review because Europe, including the U.K., as well as the rest of the world is in a slow growth mode. This could lead to a recession within two years and a decline in stock markets. While the markets could run higher here, Edward and Jill had concerns about being all in stocks since they knew this could impact their Peak Life Style, but they felt they didn't have any options. A difficult decision had to be made. To help them, we looked at the impact of a 20% decline in stocks on their portfolio and along side a rebalanced one with 60% in stocks.

20% Decline on \$2,000,000 Portfolio		
	Before %	Rebalanced %
Stocks	100	60
Fixed Income	0	40
Decline in \$	\$400,000	\$240,000

Edward and Jill opted to reduce their stock weighting from 100% to 60% over the near term. This decision will help reduce their exposure to a potential stock market decline almost by half in terms of dollars. They felt much more at ease since they realized they didn't need the extra risk in their portfolio. For explanation of PRFER see page 2.

How to plan for surprises since... they always happen

Brexit serves as a timely reminder to re-evaluate your life style and your portfolio. Paradoxically, as a response to slow growth, very low interest rates have boosted real estate and stock prices rather than sustainable growth, making investors' Peak Life Styles like Edward and Jill's look good *on paper* until it was reassessed. **If you don't have a simple, understandable asset allocation framework, want a second opinion on your portfolio or are interested in learning more about your Peak Life Style, please connect with me.**

Mark Pearlstein | T. 416-733-5257 | F. 416-733-5250 | mark.pearlstein@rbc.com



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THE PRFER EXPLAINER

PRFER

Pearlstein Relative Fixed Equity Ratio

Safety	30%
Vary	40% ↕
Growth	30%

PRFER: is a simple framework for asset allocation that takes into account an investor's preference for risk - the chance that an investment's return will be different than expected - and the ups and downs of the markets. How much risk do you want to take to achieve your investment goals?

SAFETY BUCKET: Includes bonds, GICs, savings accounts and cash because it generates safe interest income. On maturity you receive your principle back plus interest. Your principle and income are safe, but not against future inflation.

GROWTH BUCKET: Includes stocks representing partial ownership in a publicly traded company. As a part owner you receive dividend income that can grow over time in addition to the value of stock owned.

Dividends and stock prices are not guaranteed but they do provide partial protection against future inflation. This is why stocks over very long periods of time have done better than fixed income by a wide margin.

Good Market Conditions

▪100% GROWTH

Negative Market Conditions

▪100% SAFETY

If you knew times were always going to be good, you'd place all your liquid investments in Growth. On the other hand, if you knew times were always going to be bad, you'd place all of your liquid investments in Safety.

The problem is no one knows what is going to happen in your personal situation or the economy. So, the best place to start is 50% SAFETY and 50% GROWTH. The next step is to ask how much risk do you want to take.

To begin to answer this question, the asset allocation framework that works best is to place at least 30% in SAFETY, 30% in GROWTH and the balance of the remaining 40% VARIES depends on two additional questions:

What is going on in your life at the ground level? For example, your age and your investment time horizon.

What is happening in the capital markets; are conditions good or bad?

PRFER is a flexible framework that changes when you and the markets do. Reviewing it at least on annual basis keeps you focused on your investment goals and provides peace of mind.

Please connect with Sam Kim at 416-733-5246 or sam.kim@rbc.com for more information.



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